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**RESEARCH
NOTES:**

Project 539

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Third Party Transaction Cost-Benefit Analysis

Background

The Arizona Department of Transportation (ADOT), Arizona Transportation Research Center (ATRC), selected consultants from Data Site Consortium, Inc., to perform a cost-benefit study of the Motor Vehicle Division's (MVD) Third Party Program. The Third Party Program is a tool of competitive government that allows MVD to improve service quality and enhance customer service and satisfaction. ATRC and MVD desired a study to quantify the benefits and cost savings of third parties in offloading work and expense from MVD. This is particularly important as the potential increases for third parties to grow, and continued emphasis is placed on budget management and reducing wait times in MVD offices.

The project scope included a comprehensive analysis of direct and indirect costs of transacting business in third parties versus MVD field offices, including long term and short term costs. The analysis includes examining the third party process in detail and comparing it with the same process within MVD operations to

determine the cost to MVD of providing a transaction through a third party versus the cost to provide the same transaction in an MVD office.

Approach & Findings

The methodology employed two lines of inquiry. The first was an analysis of the current models to identify gaps and shortcomings. The second involved querying persons familiar with the problem. This included officials in other states who were asked to complete a survey and officials in Arizona who were interviewed in more depth. The findings for each method were as follows:

Gaps in Current Models:

Our objectives when studying the current Third Party Cost-Benefit models and literature were to:

- Obtain and review available Third Party Cost-Benefit models prepared for MVD.
- Conduct a search and review of available literature related to the costing of internally and externally

performed MVD third-party transactions.

- Perform a gap analysis of the existing models by examining current best-practices.

Our analysis of current models and literature disclosed the following gaps and understandings:

- Full cost allocation is the common method used in performing privatization/outsourcing cost analyses.
- The complexity of transactions and services provided by MVD and Third Parties varies significantly.
- Several channels are used to deliver these services (Internet, mail, over the counter, and phone).
- A better means of identifying the benefits of the Third Party Program should be determined.
- Hard dollar cost savings should not be the sole determinant of value of the Third Party Program.

Interview and Survey Results:

The primary purpose of the interviews with MVD staff was to obtain a greater understanding of the business processes, transactions and resources employed to deliver MVD services by field offices and through the Third Party Program. Secondly, we endeavored through our interviews to gain a better understanding of the issues associated with the previous cost models and how we could improve on the past models.

All interviewees agreed that attempting to do a study on comparing costs of the Third Party Program to the costs of

MVD delivered services is a difficult and complex endeavor. Nearly half of those interviewed had reviewed the previous Third Party cost models that had been prepared by MVD. All interviewees that reviewed the past models did not completely agree with the way in which the transaction costs had been derived and had suggestions on ways to improve the models. A full cost approach for arriving at MVD Customer Service costs was almost unanimously stated as the preferred technique. Intuitively, most interviewees agreed that some type of classification scheme for transactions would make comparing transaction costs more meaningful. Although most did not suggest an approach, there was unanimous agreement of those familiar with previous modeling efforts that some type of classification by delivery channel would be appropriate. These channels would include mail, phone, Internet and over the counter transactions

Implementation

Using lessons learned from the review of prior models, review of relevant literature, and interviews with key personnel, a Third Party Transaction Cost model was constructed, populated with relevant data, and analyzed. This Third Party Transaction Cost model is a series of three interlinked Microsoft Excel workbooks. Minimal Microsoft Excel knowledge is needed to use the model.

Utilizing the model and cost and transaction data for the most recent fiscal year for which data were available (July 1, 2001 – June 30, 2002); the table below shows a summary of costs per transaction by Channel: MVD Customer Service (over-the-counter), Renew-by-Mail (mail), traditional Third Party (third party offices), and Service Arizona (Internet).

General Assumptions:

- The Cost Model is based on a full cost allocation basis
- All indirect costs were included and allocated as appropriate
- The complexity of transactions and services provided by MVD and Third Parties varies significantly; however due to unavailability of data, we were unable to classify or segregate transactions by type or complexity.
- The costs indicated for Third Party reflect the state costs only and do not include individual third party office operating costs.
- Convenience fees that third parties charge their customers were not included.
- Revenues generated by MVD for Vehicle License Tax (VLT) and other transaction fees (registration fees, driver license fees, etc.) were not included in the analysis.
- Transaction types included registration renewals, titles, drivers licenses and vehicle inspections.
- Inquiry transactions such as motor vehicle registration (MVR) inquiries, fee to owner inquiries, address changes and “sold” notices were not included.
- Total cost per transaction for MVD Customer Service is \$10.66 versus \$9.54 for Third Party (savings of over \$2.1 million per year).
- Direct Personnel Costs is the largest component of the MVD Customer Service cost at 56% of the total.
- The Third Party Fees, consisting of the Retainage of 2% of VLT, Transaction Fee Retainage, and Credit Card Reimbursement is the largest component of the Third Party cost at 62%.
- In addition to the cost savings of the Third Party Program, the Program provides a number of significant intangible benefits, such as:
 - Reduced wait times in existing Customer Service offices
 - More convenient hours and days of service availability
 - Reduced customer travel time and improved customer goodwill
 - Reduced need for new buildings, MVD staff, and equipment
 - Improved image of MVD responsiveness
 - Process improvement
 - Demonstrated success of e-government and private/public partnerships.

Findings

Based on our analysis of the cost model, we are able to make the following observations:

Table 3 – Cost Model Summary

Cost Type	MVD Customer Service		Third Party	
	FY2002 Total	Cost Per Transaction	FY2002 Total	Cost Per Transaction
Direct Personnel Costs				
Customer Service Personnel	\$ 29,579,207	\$ 5.56	\$ 1,794,035	\$ 0.94
Direct Support Personnel	\$ 2,482,167	\$ 0.47	\$ 257,189	\$ 0.13
Total Direct Personnel Costs	\$ 32,061,374	\$ 6.02	\$ 2,051,224	\$ 1.07
Operating Costs				
Operating Costs	\$ 9,416,391	\$ 1.77	\$ 1,937,518	\$ 1.01
Technology Costs				
Information Technology Costs	\$ 2,950,362	\$ 0.55	\$ 1,044,921	\$ 0.55
Telecommunications Costs	\$ 1,460,780	\$ 0.27	\$ 524,581	\$ 0.27
Total Technology Costs	\$ 4,411,142	\$ 0.83	\$ 1,569,502	\$ 0.82
Indirect Costs				
MVD Indirect Costs	\$ 1,824,832	\$ 0.34	\$ 655,315	\$ 0.34
ADOT Indirect Costs	\$ 4,428,981	\$ 0.83	\$ 252,765	\$ 0.13
State Indirect Costs	\$ 250,110	\$ 0.05	\$ 14,274	\$ 0.01
Total Indirect Costs	\$ 6,503,922	\$ 1.22	\$ 922,354	\$ 0.48
Building & Equipment Costs				
Building Costs	\$ 2,074,994	\$ 0.39	\$ 118,421	\$ 0.06
Equipment Costs	\$ 1,868,629	\$ 0.35	\$ 106,644	\$ 0.06
Total Building & Equipment Costs	\$ 3,943,623	\$ 0.74	\$ 225,065	\$ 0.12
Other Costs				
Other Costs	\$ 384,098	\$ 0.07	\$ 137,933	\$ 0.07
Third-Party Fees				
Third-Party Fees	N/A	N/A	\$ 11,382,322	\$ 5.96
Total Costs	\$ 56,720,549	\$ 10.66	\$ 18,225,918	\$ 9.54
Total Cost Savings Using Third Parties			\$ 2,142,993	\$ 1.12

The full report: *Third Party Transaction Cost-Benefit Analysis* by Mike Keeling, Steve Kalina and Don Logue, Data Site Consortium, 1 East Camelback Road, Suite 660, Phoenix, AZ 85012 (Arizona Department of Transportation, report number FHWA-AZ-03-539, published April 2003) is available from the Arizona Transportation Research Center, 206 S. 17 Ave., mail drop 075R, Phoenix, AZ 85007; phone 602-712-3138.